In the Supreme Court of the United States

OCTOBER TERM, 1966

No. 673

COMMISSIONER OF INTERNAL REVENUE, PETITIONER

v.

ESTATE OF HERMAN J. BOSCH, DECEASED, IRVING TRUST COMPANY, EXECUTOR

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

REPLY BRIEF FOR THE PETITIONER

In this brief, we reply to respondent's three principal arguments: (1) the non-adversary rule is unworkable and respondent's proposed rule is easier of application, (2) the *Freuler* decision does not support the non-adversary rule, and (3) the pertinent Regulations do not support the non-adversary rule.

1(a) Respondent argues that the non-adversary rule should be rejected because it is not easy to draw a sharp distinction between adversary and non-adversary proceedings. The courts, however, regularly are called upon to draw lines on the basis of criteria that are no more, and are often less, precise—concepts such as due care and unreasonable restraint

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of trade pose substantially the same problem—but that has not prevented the courts from effectively utilizing such standards in deciding legal issues. For it is a commonplace that an otherwise proper standard is not to be rejected because of difficulty in drawing the line in close cases. As Justice Holmes once said, "Neither are we troubled by the question where to draw the line. That is the question in pretty much everything worth arguing about in the law." *Irwin* v. *Gavit*, 268 U.S. 161, 168.

Moreover, in many cases, such as this one, the facts will leave little room for doubt as to which side of the line the case falls. Whenever, as here, there was no controversy between the parties (all of whom urged the State court to adopt the same position) and only one side of the issue was presented (that which would result in the hoped-for tax reduction), it is clear that the proceeding was non-adversary and that an erroneous decree rendered in such circumstances should not have conclusive effect for tax purposes.

The non-adversary approach does not, as respondent suggests, require that the proceedings be "belligerent," but only that a State trial court decree must adjudicate a dispute between the parties, not merely ratify the parties' unanimous contention if it is to control federal tax consequences. There is no legitimate reason why a taxpayer who has initiated a suit in a State trial court and then declined "to actively litigate an issue" in that court (Resp. br. 7) should thereby bar the Com-

missioner from litigating that issue in a federal tax case.[1]

(b) Nor does respondent propose a clear-cut standard by which to gauge the effect of a State trial court decree in a federal tax suit. Respondent argues that a State decree is binding if it is "an authoritative decision" (Br. 9). In deciding this question, respondent suggests that the federal courts should consider, *inter alia*, the following factors: whether the State trial court gave the issue "serious attention," whether the State court made "an independent determination," and whether (and to what extent) the State trial court's decision is entitled to "precedential value" (Br. 9). Such a standard is certainly no easier to apply—or more likely to produce sound results—than the non-adversary test which the vast majority of the appellate courts are now using without unusual difficulty.[2]

Respondent also suggests that the federal court should consider whether all interested parties had appeared, whether briefs had been submitted, and whether oral argument had been made. Formalities,

[1] Respondent argues that the non-adversary rule might tax a beneficiary "on that which he did not possess" (Br. 7). The estate tax, however, is levied upon the estate, not upon the beneficiary. Therefore, a beneficiary who relinquished his right to receive a bequest would not be subject to any tax.

[2] For example, the "precedential value" to be accorded the decision would presumably depend upon such factors as the status of the court, the reputation of the judge, the significance of the issue decided, and, perhaps most important, the cogency of the judge's analysis of the issue. The other factors proposed by respondent, such as whether the court gave the issue "serious attention" and made "an independent determination," are no easier to apply.

however, give no assurance that the proceeding is anything more than an instrument of tax avoidance—for these criteria would be met if all the parties urged the same result, cited the same authorities, and adopted the same position throughout, as was true in the instant case.

(c) Even respondent agrees that *factual* determinations made by a State trial court are not binding in a federal tax case if the State proceedings were non-adversary (Br. 8). The reason respondent gives for refusing to follow non-adversary *factual* determinations—the State trial court may "not be aware of evidence" unless presented by the parties (Br. 8)— applies equally to *legal* determinations resulting from non-adversary proceedings. Where the parties have adopted a unanimous position as to a legal issue, a busy State trial judge is hardly likely to undertake exhaustive independent research. His professional bias is to reserve his energy for disputed questions. Thus, the trial court may not be aware of pertinent legal authorities unless brought to its attention by the parties. For example, in the companion *Second National Bank* case, the probate court rendered its decision approving the uncontested proration as proposed by the executor on the same day that it received the guardian's memorandum, and apparently without consideration of the uncited State decisions which would have required the opposite conclusion (see our brief in *Second National,* p. 21).

Moreover, no function would be served by requiring that the effect given a State trial court decree turn on whether the issue decided was factual or legal—

the possibilities of tax avoidance are the same in either case. The Sixth Circuit has rejected just such a distinction. In *Stark* v. *United States,* 351 F. 2d 160 (C.A. 6), certiorari denied, 384 U.S. 939, the court unequivocally refused to follow an erroneous factual finding reached by a State probate court in a non-adversary proceeding. A short time later, it rejected a taxpayer's argument that the rule should be different where the question was the effect of a State trial court's legal conclusion rather than its factual finding, stating that in *Stark* it had "rejected a somewhat similar effort" to "employ a non-adversary Probate Court proceeding in order to achieve post-death estate tax planning." *Old Kent Bank and Trust Co.* v. *United States,* 362 F. 2d 444, 450 (C.A. 6).

(d) Respondent cites *Daine* v. *Commissioner,* 168 F. 2d 449, 452 (C.A. 2), for the proposition that a sovereign is not "likely to permit its revenue to be set at naught through such retroactive manipulation of state judicial proceedings" and agrees that a State trial court "determination * * * which purports to have a *nunc pro tunc* effect" should not be followed (Br. 8). Yet that is precisely the effect that it seeks to attribute to the non-adversary decree of the instant New York trial court. As explained in our main brief in this case (p. 12, fn. 8, and p. 26, fn. 21) and in our brief in the *Second National* case (pp. 13–16), a non-adversary State trial court decision that decedent's widow rather than his son owns certain property included in decedent's estate is conclusive on the federal government *prospectively, i.e.,* from the date of the decree, just as if the son had made a gift of the

property to his mother at that time. All we seek to do here is deny such non-adversary decree *retroactive* effect as a determination that the widow received the property from decedent at the time of his death, rather than after his death through relinquishment by the son of his rights. (See *ibid.*)

(e) Respondent argues that the State decree should be binding in this case because (as it contends) the State accounting proceeding was necessary in order to protect the trustee should decedent's widow, at her death, appoint outside of the class as limited by her release (Br. 6–7). Respondent makes this argument although (1) the release left her free to appoint to anyone in the world except herself, her estate, her creditors or the creditors of her estate (R. 39), (2) there was no existing dispute between any of the parties as to the scope of the widow's rights,[3] (3) the State proceeding was "prompted" not by the trustee's desire for protection but by the federal tax controversy (R. 10), (4) the trustee "had not filed an accounting since the trust had been created 33 years before" (Resp. br. 6), and (5) the trustee would have been completely protected if it had waited until the widow's death and then, in the unlikely event that she appointed the property to one of the prohibited class, declined to make distribution until it had tested the legal question here presented. Even if there were some basis for claiming that the accounting was necessary, we would urge that it does not bind the federal tax authorities when the parties, instead of having litigated

[3] So far as the record shows she had no intent to appoint to her estate or her creditors.

their rights, merely sought judicial ratification of their unanimous agreement.

2. Respondent next contends that *Freuler* v. *Helvering,* 291 U.S. 35, precludes this Court from adopting the non-adversary approach because that case is authority for the proposition that "a federal court is bound by a non-adversary State court determination" (Br. 10). That contention is without merit. In *Freuler,* this Court was concerned with a special section of the Revenue Act of 1921 (repealed in 1924) which provided that trust beneficiaries were taxable on income which was distributable according to an "order governing the distribution."[4] Reasoning that Congress intended, by this language, to give effect to "the order of the court having jurisdiction of the trust" (p. 44), this Court held that a distribution order of a State trial court having jurisdiction over the trust was determinative. Thus, even if respondent has correctly interpreted *Freuler,* it would not be binding in this case dealing not with the unusual 1921 statute, but with the marital deduction, as to which the governing statute makes no reference to any court decree. (See also the legislative history, long-standing Regulations, and policy consideration discussed in our main brief, pp. 13–18, 27–30.)

However, despite the specific language of the unusual 1921 statute involved in *Freuler,* the Court did not reject the government's argument that a State trial court order should not be followed if rendered in a non-adversary proceeding brought to reduce taxes.

[4] Revenue Act of 1921, c. 136, 42 Stat. 227, § 219(d), repealed by Revenue Act of 1924, c. 234, 43 Stat. 253, § 219.

Instead, this Court considered on the merits the government's argument that a State trial court decree would not be binding if "all the parties [had] joined in a submission of the issues and sought a decision which would adversely affect the Government's right to additional income tax" (*id.* at 45); it rejected that argument as *factually* inapplicable in *Freuler,* noting *inter alia* that some of the beneficiaries had filed objections to approval of the trustee's account. Whether this Court was correct in concluding that the State court proceedings in *Freuler* were sufficiently adversary to satisfy the unusual statute involved in that case is not relevant here; the significant point for present purposes is that the non-adversary approach was not rejected. Since that approach is supported by the legislative history of the marital deduction provision, by longstanding administrative practice, by the Regulations, and by the majority of the courts of appeals, it is appropriate for this Court now to adopt it.

3. Respondent argues that the two pertinent Regulations do not support the non-adversary rule because they "suggest that certain non-adversary proceedings will be accepted" (Br. 16). The Regulations merely indicate that if a State court decree is correct, it will be accepted regardless of whether it was rendered in an adversary or a non-adversary proceeding, but that a decree which is erroneous, *i.e.,* one which is "at variance with [State] law," will be accepted only if rendered "in an adversary proceeding following a genuine and active contest," *i.e.,* only if it is not "a mere

cloak for a gift."[5] Therefore, these two Regulations (one of which has remained substantially unchanged since 1919 and the other since 1949) strongly support the non-adversary approach.

Respectfully submitted.

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[5] Quotations are from Treas. Regs. § 20.2053–1(b)(2) and § 20.2056(e)–2(d)(2), which are reproduced at pp. 42–43 of the Appendix to our main brief and discussed at greater length at pp. 16–18 of that brief.

*In lieu of the Solicitor General who has disqualified himself.

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